

CHAPTER 1

WHAT IS STRATEGY and WHY IS IT IMPORTANT?

Crafting & Executing

STRATEGY

THE QUEST FOR COMPETITIVE ADVANTAGE

Concepts and Cases

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Learning Objectives



THIS CHAPTER WILL HELP YOU UNDERSTAND:

- LO 1** What we mean by a company's *strategy*.
- LO 2** The concept of a *sustainable competitive advantage*.
- LO 3** The five most basic strategic approaches for setting a company apart from rivals and winning a sustainable competitive advantage.
- LO 4** That a company's strategy tends to evolve because of changing circumstances and ongoing efforts by management to improve the strategy.
- LO 5** Why it is important for a company to have a viable business model that outlines the company's customer value proposition and its profit formula.
- LO 6** The three tests of a winning strategy.

CORE CONCEPT

A company's **strategy** is the set of actions that its managers take to outperform the company's competitors and achieve superior profitability.

WHAT DO WE MEAN BY *STRATEGY*?

- ◆ What is our present situation?
 - Business environment and industry conditions
 - Firm's financial and competitive capabilities
- ◆ Where do we want to go from here?
 - Creating a vision for the firm's future direction
- ◆ How are we going to get there?
 - Crafting an action plan for heading the firm in the intended direction, staking out a market position, attracting customers, achieving the targeted financial and market performance, and getting the firm where it wants to go is its *strategy*.

WHAT IS STRATEGY ABOUT?

- ◆ Strategy is all about **How**:
 - **How** to attract and please customers.
 - **How** to compete against rivals.
 - **How** to position the firm in the marketplace to capitalize on attractive opportunities for growth.
 - **How** to respond to changing economic and market conditions.
 - **How** to manage each functional piece of the business.
 - **How** to achieve the firm's performance targets.

STRATEGIC MANAGEMENT PRINCIPLE

- ◆ Strategy is about competing differently from rivals—doing what competitors don't do or, even better, doing what they cannot do!

WHY BOTHER WITH STRATEGY?

- ◆ A firm needs a strategy to specify what actions are going to be taken:
 - To improve its financial performance.
 - To strengthen its competitive position.
 - To gain a sustainable competitive advantage over its market rivals.
- ◆ A creative, distinctive strategy:
 - Helps produce above-average profits.
 - Increases competitive pressures on rivals.

STRATEGY AND COMPETITORS

- ◆ Strategy is about competing differently from rivals—
 - Doing what they *do not* do or doing it better!
 - Doing what they cannot do!
 - Doing things in ways that attract customers and set a firm apart from its rivals.
 - Doing things in a manner calculated to produce a competitive edge over rivals.
 - Knowing what the firm must do and also what it must not do.

FIGURE 1.1 Identifying a Company's Strategy—What to Look For

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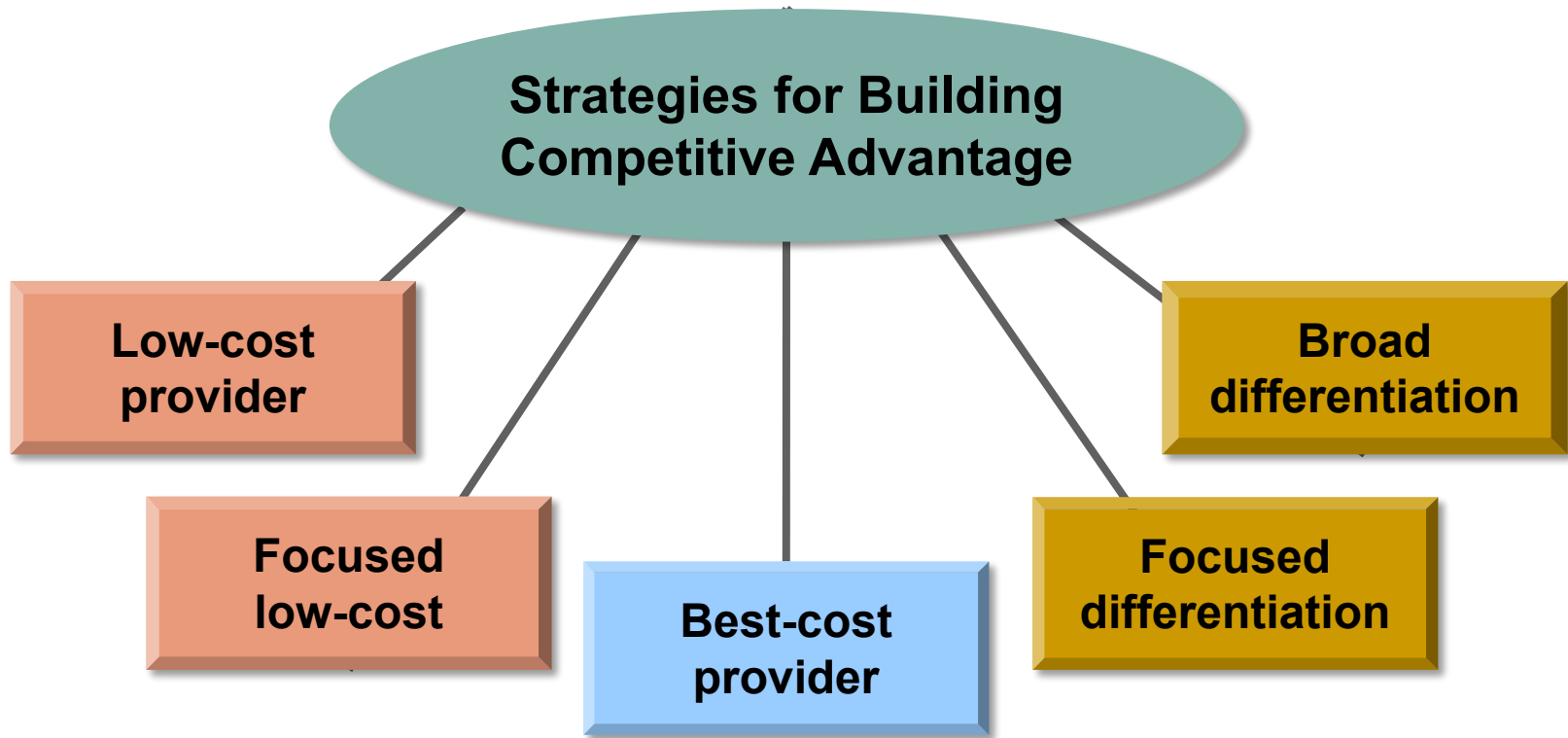


- ◆ **Key elements of Starbucks's strategy:**
 - Train “baristas” to serve a wide variety of specialty coffee drinks that allow customers to satisfy their individual preferences in a customized way.
 - Emphasize store ambience and elevation of the customer experience at Starbucks stores.
 - Purchase and roast only top-quality coffee beans.
 - Foster commitment to corporate responsibility.
 - Expand the number of Starbucks stores domestically and internationally.
 - Broaden and periodically refresh in-store product offerings.
 - Fully exploit the growing power of the Starbucks name and brand image with out-of-store sales.

STRATEGY AND THE QUEST FOR COMPETITIVE ADVANTAGE

- ◆ **Competitive Advantage**
 - Requires meeting customer needs either more **effectively** (with products or services that customers value more highly) or more **efficiently** (by providing products or services at lower cost).
- ◆ **Sustainable Competitive Advantage**
 - Requires giving buyers **lasting** reasons to prefer a firm's products or services over those of its competitors.

BASIC STRATEGIC APPROACHES



STRATEGIC APPROACHES

- ◆ **Building a competitive advantage by:**
 - Striving to become the industry's low-cost provider (efficiency).
 - Outcompeting rivals on differentiating features (effectiveness).
 - Offering the lowest (best) prices for differentiated goods (best-cost provider).
 - Focusing on better serving a niche market's needs (efficiency and/or effectiveness).

CORE CONCEPT

- ◆ A firm achieves a **competitive advantage** when it provides buyers with superior value compared to rival sellers or offers the same value at a lower cost to the firm.
- ◆ The firm achieves a **sustainable competitive advantage** if its advantage persists despite the best efforts of competitors to match or surpass its advantage.

GAINING SUSTAINABLE COMPETITIVE ADVANTAGE

- ◆ How to create a sustainable competitive advantage:
 - Develop valuable expertise and competitive capabilities over the long-term that rivals cannot readily copy, match or best.
 - Put the constant quest for sustainable competitive advantage at center stage in crafting your strategy.

WHY A COMPANY'S STRATEGY EVOLVES OVER TIME

- ◆ Managers modify strategy in response to:
 - Changing market conditions
 - Advancing technology
 - Fresh moves of competitors
 - Shifting buyer needs
 - Emerging market opportunities
 - New ideas for improving the strategy

STRATEGIC MANAGEMENT PRINCIPLE

- ◆ Changing circumstances and ongoing management efforts to improve the strategy cause a company's strategy to evolve over time—a condition that makes the task of crafting strategy a *work in progress*, not a one-time event.
- ◆ A company's strategy is shaped partly by management analysis and choice and partly by the necessity of adapting and learning by doing.

THE EVOLVING NATURE OF A FIRM'S STRATEGY

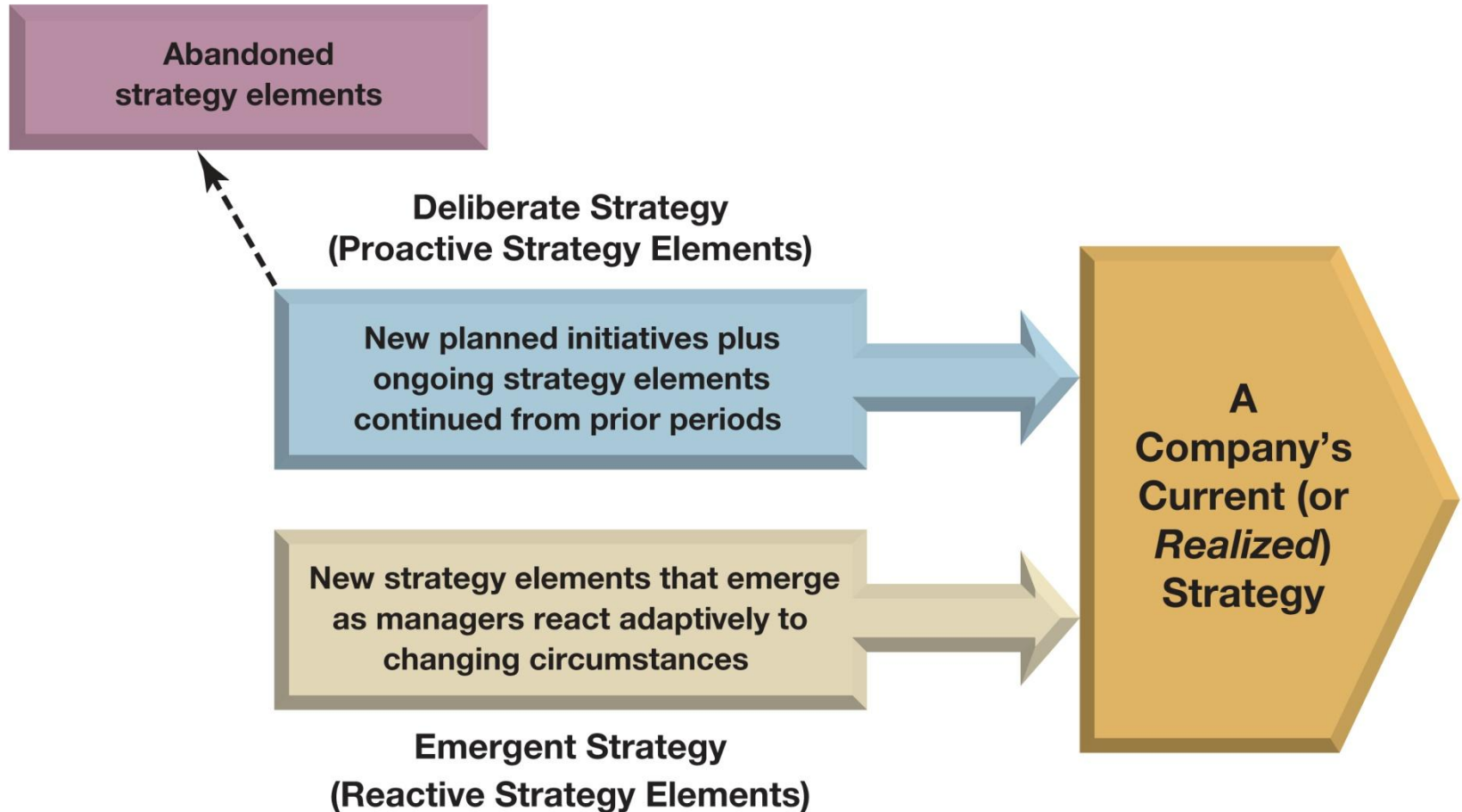
- ◆ Realized (current) strategy is a blend of:
 - Proactive (deliberate) strategy elements that include both continued and new initiatives.
 - Reactive (emergent) strategy elements that are required due to unanticipated competitive developments and fresh market conditions.

CORE CONCEPT

- ◆ A company's **deliberate strategy** consists of proactive strategy elements that are both planned and realized as planned; its **emergent strategy** consists of reactive strategy elements that emerge as changing conditions warrant.

FIGURE 1.2 A Company's Strategy Is a Blend of Proactive Initiatives and Reactive Adjustments

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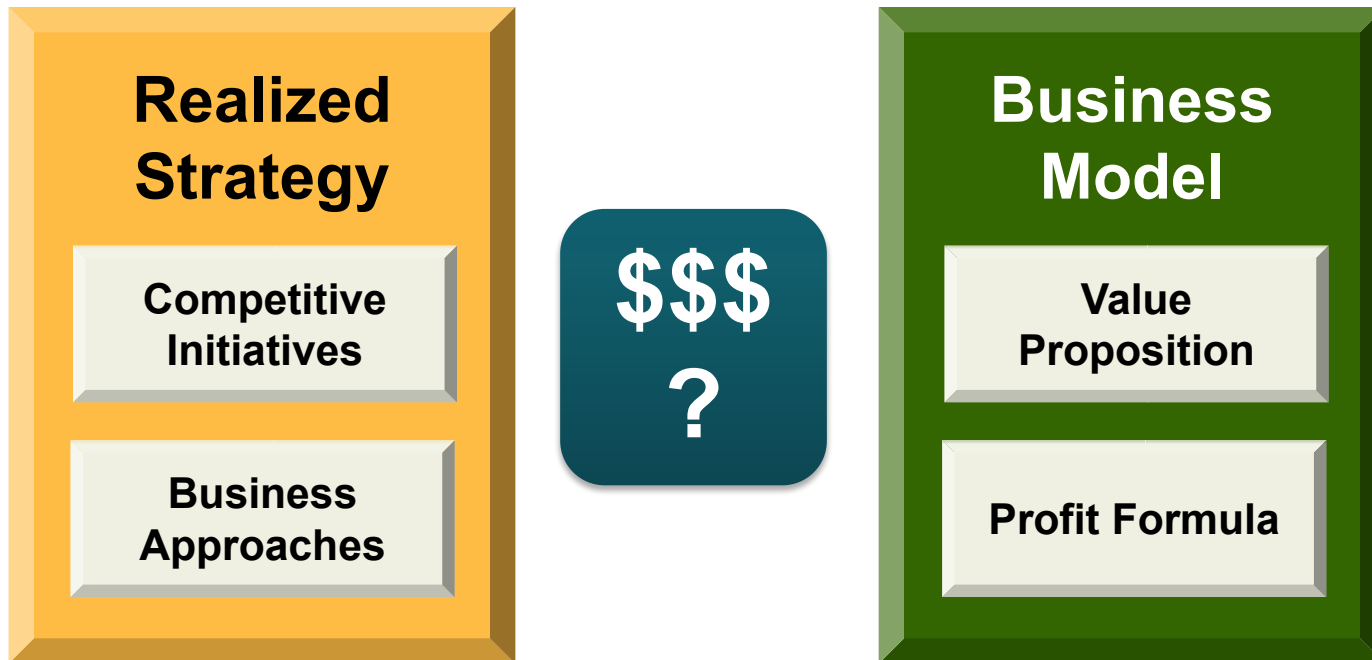


THINKING STRATEGICALLY

◆ Just for Fun:

- Using the terms shown in Exhibit 1.2, explain why U.S. football teams get four downs to make a first down.
- How does risk affect play selection (strategy) as a team fails to advance on each of its four downs?
- What rules of play in other sports affect how the basic principles of strategy are applied to game play?

THE RELATIONSHIP BETWEEN A FIRM'S STRATEGY AND ITS BUSINESS MODEL



A COMPANY'S STRATEGY AND ITS BUSINESS MODEL

- ◆ How the business will make money :
 - By providing customers with value.
 - ❖ The firm's *customer value proposition*
 - By generating revenues sufficient to cover costs and produce attractive profits.
 - ❖ The firm's *profit formula*

It takes a proven business model—one that yields appealing profitability—to demonstrate viability of a firm's strategy.

CORE CONCEPT

- ◆ A company's **business model** sets forth the logic for how its strategy will create value for customers, while at the same time generate revenues sufficient to cover costs and realize a profit.

BUSINESS MODEL ELEMENTS

◆ The Customer Value Proposition

- Satisfying buyer wants and needs at a price customers will consider a good value.
- ❖ The greater the value provided (V) and the lower the price (P), the more attractive the value proposition is to customers.

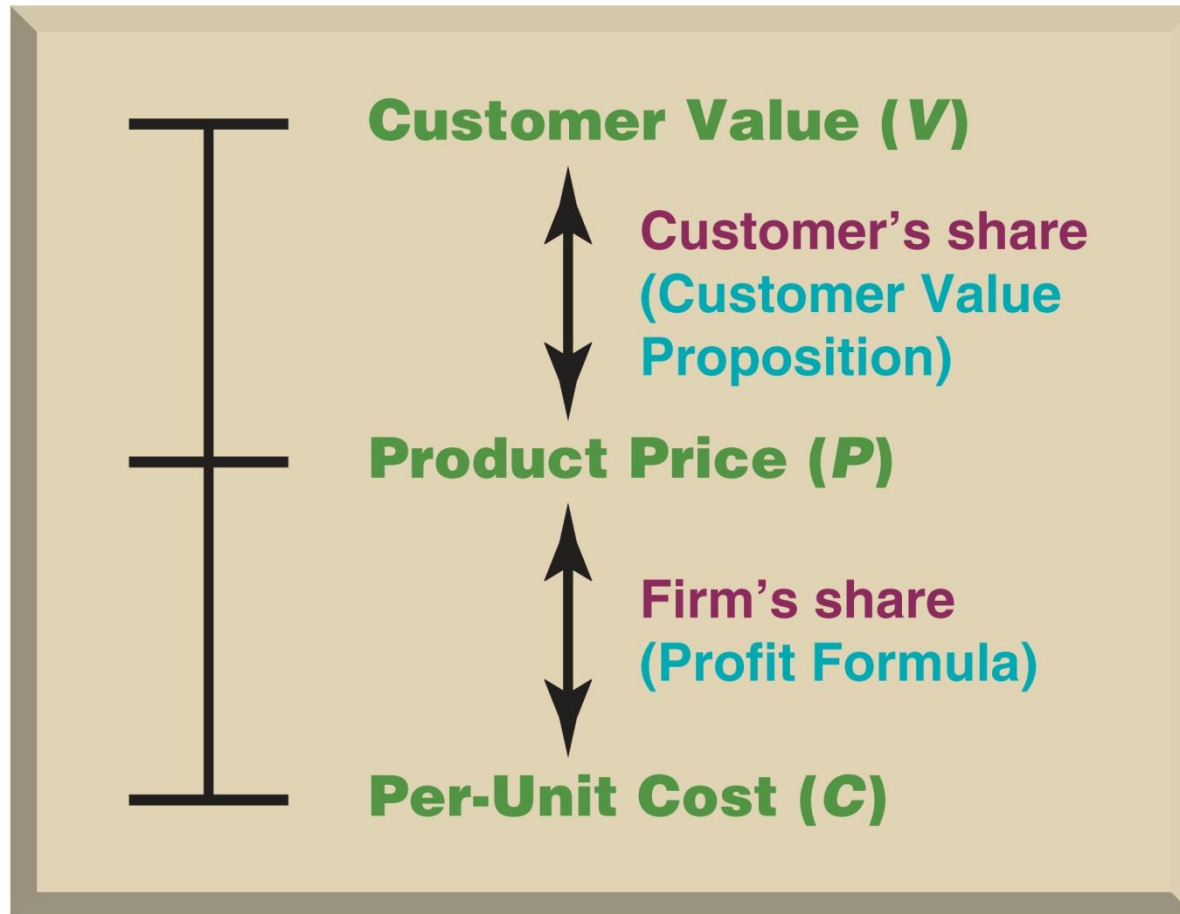
BUSINESS MODEL ELEMENTS (CONT'D)

◆ The Profit Formula

- Creating a cost structure that allows for acceptable profits, given that pricing is tied to the customer value proposition.
 - ❖ V —the value provided to customers
 - ❖ P —the price charged to customers
 - ❖ C —the firm's costs
- The lower the costs (C) for a given customer value proposition ($V-P$), the greater the ability of the business model to be a moneymaker.

FIGURE 1.3 The Business Model and the Value-Price-Cost Framework

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THINKING STRATEGICALLY

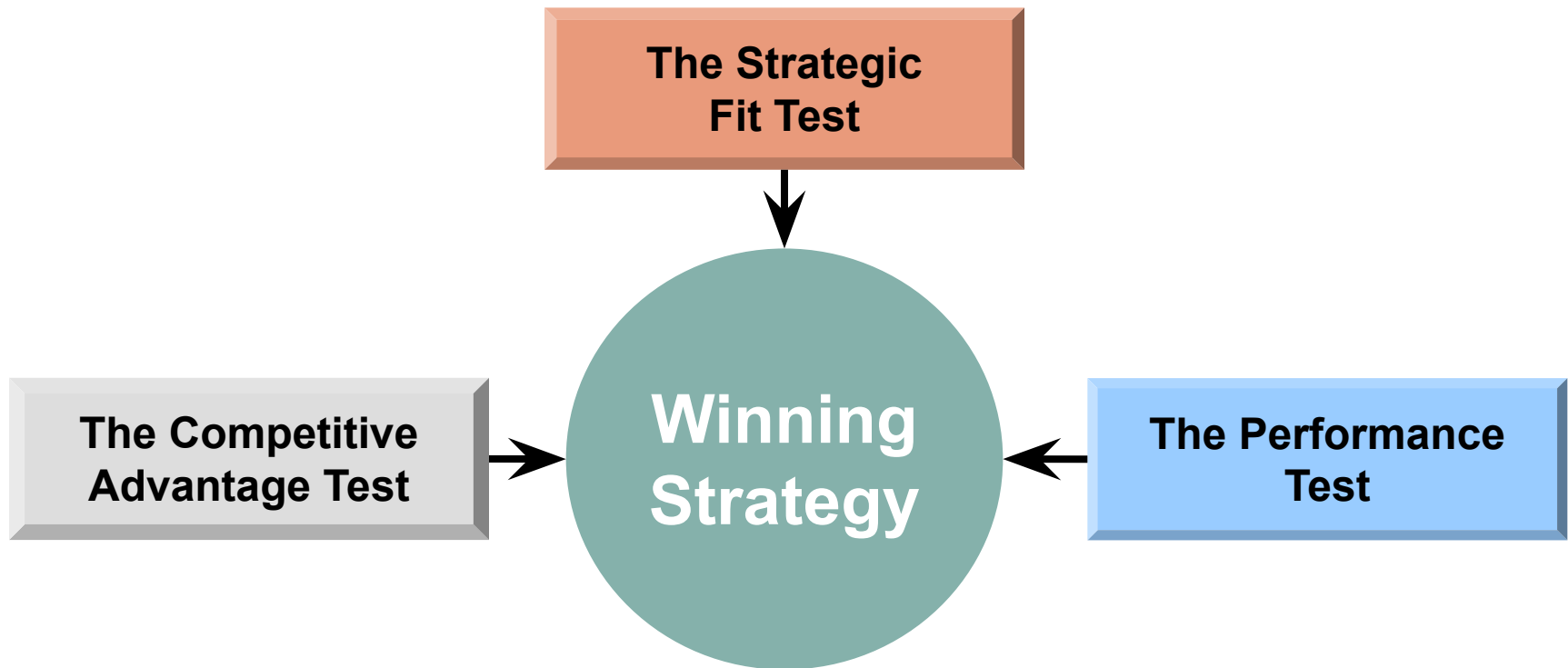
- ◆ Amazon's continuing lack of profitability has begun to concern its long-term investors.
 - What internal and external factors could be contributing to the lack of profitability?
 - How could the problem be explained in terms of changes in the value, price, and cost factors associated with Amazon's business model?
 - What must Amazon do now to create a business model that is sustainable over the long term?



◆ Who listens to the radio anymore?

- Given the changes in how people listen to music, are the business models of Pandora, Sirius XM and over-the-air broadcasters viable over the long term?
- Which competitor's present strategy best passes the three tests of a winning strategy?
- What internal and external factors will create particular difficulties for each competitor in changing its strategy or business model?

IS OUR STRATEGY A WINNER?



WHAT MAKES A STRATEGY A WINNER?

- ◆ A winning strategy must pass three tests:
 - The Fit Test
 - ❖ Does it exhibit dynamic fit with the external and internal aspects of the firm's overall situation?
 - The Competitive Advantage Test
 - ❖ Can it help the firm achieve a significant and sustainable competitive advantage?
 - The Performance Test
 - ❖ Can it produce good performance as measured by the firm's profitability, financial and competitive strengths, and market standing?

WHY CRAFTING AND EXECUTING STRATEGY ARE IMPORTANT TASKS

- ◆ **Strategy provides:**
 - A prescription for doing business.
 - A road map to competitive advantage.
 - A game plan for pleasing customers.
 - A formula for attaining long-term standout marketplace performance.

*Good Strategy + Good Strategy Execution =
Good Management*

STRATEGIC MANAGEMENT PRINCIPLE

- ◆ How well a company performs is directly attributable to the caliber of its strategy and the proficiency with which the strategy is executed.

THINKING STRATEGICALLY

- ◆ Google's web browser-based Chrome operating system and its online applications suite are now challenging Microsoft's long-term dominance of those marketplace sectors.
- ◆ What should be Microsoft's first response to this competitive challenge?
- ◆ How will Microsoft's response to this competitor's actions affect its business model?
- ◆ Which competitor's strategy will likely be the eventual winner in the marketplace? Why?

THE ROAD AHEAD

- ◆ Strategy is about asking the right questions:
 - What must managers do, and do well, to make a firm a winner in the marketplace?
- ◆ Strategy requires getting the right answers:
 - Good strategic thinking and good management of the strategy-making, strategy-executing process.
 - First-rate capabilities and skills in crafting and executing strategy are essential to managing successfully.
- ◆ *Welcome and best wishes for your success!*